

UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF ALABAMA

In Re

WILLIAM C. SPOTSWOOD, IV  
SHERRI S. SPOTSWOOD

Case No. 02-12922-MAM-7

Debtors.

FIRST GULF BANK

Plaintiff,

v.

Adv. No. 02-1143

WILLIAM C. SPOTSWOOD, IV

Defendant.

**ORDER DETERMINING CERTAIN OF DEBTOR'S  
DEBT TO FIRST GULF BANK IS NONDISCHARGEABLE**

Lionel C. Williams, Mobile, Alabama, Attorney for William C. Spotswood  
Marion E. Wynne, Fairhope, Alabama, Attorney for First Gulf Bank

This matter is before the Court on the trial of an adversary proceeding involving First Gulf Bank's complaint that William Spotswood's debt to FGB is nondischargeable under § 523(a)(6) of the Bankruptcy Code . The Court has jurisdiction to hear this matter pursuant to 28 U.S.C. §§ 157 and 1334 and the Order of Reference of the District Court. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2) and the Court has the authority to enter a final order. For the reasons indicated below, the Court finds that \$18,000 of William Spotswood's debt to First Gulf Bank is nondischargeable.

FACTS

William Spotwood is the owner of Spotwood Construction, Inc. ("Construction"), a corporation engaged in residential home and marine pier construction. On October 26, 2000

Construction entered into a loan agreement with First Gulf Bank (“FGB”) to borrow \$25,102.50; William Spotswood personally guaranteed the loan. The loan contained a security agreement under which Construction granted FGB a security interest in a 26 foot barge, a 1998 Yamaha outboard motor, and a 1987 GMC truck.

In a letter to FGB dated October 19, 2000, William Spotswood’s wife, Sherri, listed the value of the property pledged as security for the loan. The letter stated that the barge was worth \$26,200, the barge retrofit materials were worth \$1,300, the “hard-mounted” electric boom was worth \$3,500, the outboard motor was worth \$4,500, and the truck was worth \$8,900. Attached to the letter was a fax William Spotswood received from Silver Ships, Inc. that quoted a \$26,200 price for a new barge with similar specifications to the used barge Spotswood pledged as security for the FGB loan. William Spotswood testified that he offered the \$26,200 quoted price of a new barge to FGB because it was the best indicator he could give of the value of his barge. Spotswood testified that his barge was worth only approximately \$12,000 when he entered into the loan agreement with FGB on October 26, 2000 - not the “new price” because it was used. He had purchased it for \$6,700 about January or February 1999 and improved it himself.

FGB filed a financing statement covering the barge, the outboard motor, and the truck on November 16, 2000 with the Probate Judge of Baldwin County. The financing statement stated that it secured an initial indebtedness of \$25,000. FGB included the truck’s vehicle identification number (“VIN”) on the financing statement but it did not note its security interest on the truck’s certificate of title. FGB presented two witnesses who stated that they could not remember if FGB received a certificate of title on the truck when Spotswood entered into the October 26, 2000 loan agreement.

Katherine Zito was FGB's Daphne, Alabama branch manager when William Spotswood applied for the loan; she was also the loan officer who entered into the loan agreement with Spotswood. Zito testified that she could not recall if FGB received a certificate of title to the truck when the loan was made; she further stated that FGB has searched its records for the title but cannot find it. Additionally, Zito testified that FGB could not request a certificate of title to be issued to it in this situation. Vivian Houser, the custodian of FGB's records at its Robertsdale, Alabama branch, testified that she did not know if FGB ever received the truck's title either, although it is FGB's policy to get a title when making a loan secured by a vehicle.

Spotswood sold the barge, the outboard motor, the electric boom, and various other equipment associated with the barge to Wes Smith for \$20,000 on September 7, 2001 upon Smith's unsolicited offer. Spotswood testified that he intended to use the \$20,000 proceeds from the sale of the barge to pay toward the \$25,102.50 loan with FGB; however, after the events of September 11, 2001 occurred, his construction business declined and he needed to use the proceeds for his business instead.

In the bill of sale, Spotswood warranted that the barge was free of all liens and encumbrances even though he testified at trial that he knew FGB held a security interest in the barge and he knew that FGB had filed a financing statement covering the barge. Additionally, Spotswood renewed the \$25,102.50 loan with FGB on October 26, 2001 with the barge still listed as security. Tommy Faust, FGB's Daphne, Alabama vice president/market manager handled the renewal. He testified that Spotswood did not inform him that the barge listed as security on the loan had already been sold when Spotswood signed the renewal note.

Spotswood testified that he used some of the proceeds from the barge sale to make monthly payments to FGB on the loan. Spotswood stated that his home and pier construction business began to slowly improve in December 2001 and he thought he would be able to sell a house he was building around that same time and pay FGB. However, shortly thereafter one of his employees was accused of sexually harassing a woman employee at Construction. The woman filed suit against him and his wife, as owners of Construction, for letting the harassment occur.

This caused new financial problems for Spotswood. He went to see Tommy Faust regarding the financial difficulties that he and his business encountered due to the lawsuit. Faust testified that Spotswood informed him on May 2, 2002 that the barge had been sold. At the same time, Spotswood told Faust that he might have to declare bankruptcy if multiple judgments were entered against him. Faust stated that Spotswood offered a house he was building in Huntsville, Alabama as replacement collateral but FGB determined not to accept the house based on the advice of its lawyer.

Spotswood and his wife filed a joint chapter 7 bankruptcy case on May 24, 2002. Shortly after filing his bankruptcy petition, Spotswood drove the truck listed as security on the loan to FGB's Daphne, Alabama branch and offered to return it to FGB. Tommy Faust met with Spotswood and told Spotswood that because he had filed bankruptcy, Faust could not accept the truck without first talking to FGB's lawyer. Nonetheless, Spotswood left the truck parked at the Daphne, Alabama branch office and it was still there at the time of the trial of this lawsuit.

In his schedules, Spotswood listed FGB as holding a \$25,000 unsecured nonpriority claim against him based on the personal guarantee he signed on the loan FGB made to Construction. FGB initiated an adversary proceeding against Spotswood on August 22, 2002 by

filing a complaint requesting that the Court find Spotswood's entire debt to FSB is nondischargeable under § 523(a)(6) of the Bankruptcy Code. The Court held a hearing on January 21, 2003 regarding FBG's nondischargeability complaint. FGB argued that Spotswood "willfully and intentionally" sold the barge and the outboard motor without giving notice to FGB or applying the sales proceeds toward payment of its loan. Spotswood argued that he made a good faith effort to repay FGB and that he offered FGB replacement collateral after informing FGB that he had sold the barge.

### LAW

Spotswood sold a barge and an outboard motor securing FGB's \$25,102.50 loan without informing FGB of the sale. He did not use the \$20,000 in proceeds from the sale of the barge and the motor for the purpose of paying toward the loan. Instead, Spotswood invested the proceeds back into his own business before filing a chapter 7 bankruptcy case on May 24, 2002. In his schedules, Spotswood listed FGB as holding a \$25,000 unsecured nonpriority claim against him. FGB initiated an adversary proceeding against him requesting that the Court find Spotswood's debt to FGB to be nondischargeable under § 523(a)(6) of the Bankruptcy Code. FGB bears the burden of proving each element of its case by a preponderance of the evidence. *Grogan v. Garner*, 498 U.S. 279 (1991).

FGB requests that the Court find Spotswood's entire \$25,831.92 debt to be nondischargeable by his chapter 7 bankruptcy case. FGB must satisfy a two prong test under § 523(a)(6) for the Court to find that any portion of Spotswood's debt is nondischargeable. First, FGB must prove that Spotswood acted "willfully and maliciously" by selling part of FGB's security on the loan and then investing the proceeds of the sale back into his own business rather

than paying the sum toward the loan. Second, FGB must prove that it was injured by Spotswood's actions.

FGB meets the first prong of § 523(a)(6). Section § 523(a)(6) states that a debt is nondischargeable if it results from "willful and malicious injury by the debtor to another entity or to the property of another entity." 11 U.S.C. § 523(a)(6). The Bankruptcy Code does not define the term "willful and malicious." This Court previously considered the section's meaning in the *Sweet Water State Bank v. Cook (In re Cook)* case. Case No. 99-10955-MAM-7 (Bankr. S.D. Ala., September 15, 1999). The Court held that to be "willful," the "debtor must intend that the conversion of the collateral injure the creditor or the creditor's lien interest." *In re Cook* (quoting *Mitsubishi Motors Credit of America, Inc. v. Longley (In re Longley)*, 235 B.R. 651, 657 (10th Cir. BAP 1999). It further held that to be "malicious," "an act must be without justification or excuse." *Id.* (quoting *America First Credit Union v. Gagle (In re Gagle)*, 230 B.R. 174, 180 (Bankr. D. Utah 1999).

Spotswood "willfully" intended to injure FGB's lien interest by selling its security. Spotswood testified that he knew FGB's loan was secured by the barge and the outboard motor when he sold those items to Wes Smith for \$20,000 but he sold the items anyway. When Spotswood sold the items, he neither informed FGB of the sale nor used the proceeds to pay the loan. Accordingly, the Court finds that Spotswood "willfully" injured FGB.

It is also clear that Spotswood "maliciously" injured FGB because he could not offer a reasonable excuse or justification for his actions. Spotswood stated that he intended to use the proceeds to pay toward the loan but the decline of his business after September 11, 2001 led him to reconsider and invest the proceeds into his business instead. He did eventually inform FGB that he had sold the barge and the outboard motor, at which time he offered replacement

collateral to FGB. However, he did not pay any portion of the \$20,000 proceeds to FGB other than remitting some monthly payments on the loan. Moreover, his admission to FGB that he sold its security came nearly 8 months after Spotswood had signed a renewal note on his loan that still listed the barge and outboard motor as security when he knew he had already sold them. Spotswood's excuses and justifications are not reasonable or justifiable. The Court finds that he "maliciously" injured FGB.

The Court has found that Spotswood "willfully and maliciously" injured FGB by selling its security without notice and by not applying the proceeds toward payment of his loan. The Court must now determine if Spotswood's actions injured FGB, the second prong under § 523(a)(6).

FGB meets the second prong under § 523(a)(6) as well. Spotswood testified that he did not use the proceeds from the sale of the barge for the purpose of paying his loan. FGB was injured by Spotswood's actions because the sale of the barge left FGB with partial or no security for its loan<sup>1</sup>. At the filing of this case, Spotswood listed FGB as an unsecured creditor. FGB meets the second prong of the test under § 523(a)(6).

What amount of the loan is nondischargeable? Spotswood's bill of sale indicates that he received \$12,000 for the barge, \$2,500 for the outboard motor, and \$3,500 for the electric boom. All these items were part of the barge itself and they were offered as security to FGB when it made the \$25,102.50 loan to Spotswood. The Court finds that the \$18,000 Spotswood received for the sale of the barge, the outboard motor, and the electric boom is a nondischargeable debt under § 523(a)(6).

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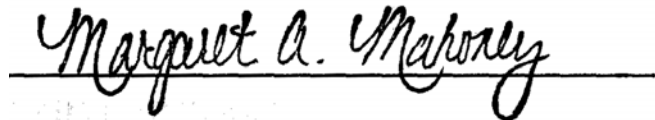
<sup>1</sup> FGB may have other collateral - the 1987 truck. The Court is not deciding whether the truck is or is not collateral subject to the FGB loan in this opinion.

The Court has found that \$18,000 of Spotswood's debt to FGB is nondischargeable under his chapter 7 bankruptcy because Spotswood "willfully and maliciously" sold 2 of the 3 items he pledged as security for the loan without first informing FBG or applying the proceeds of the sale toward the loan. Spotswood voluntarily returned the remaining item he pledged as security for the loan, his 1987 GMC truck, to FGB shortly after he declared bankruptcy.

The parties disagree regarding whether FGB properly perfected its security interest in the truck. FGB filed a financing statement that listed the truck as security but it did not note its security interest on the truck's certificate of title. The perfection issue is not before the Court at this time. The Court will not make any findings regarding FGB's security interest in the truck. There is no dischargeability issue about the debt secured by the truck because Spotswood was not alleged to have done anything willful and malicious regarding it. The Court's findings in this case are limited to the nondischargeability of Spotswood's debt which was secured by the barge and its appurtenances.

It is ORDERED and ADJUDGED that \$18,000 of William Spotswood's debt to First Gulf Bank is nondischargeable pursuant to 11 U.S.C. § 523(a)(6).

Dated: February 5, 2003

A handwritten signature in black ink, reading "Margaret A. Mahoney", is written over a horizontal line.

MARGARET A. MAHONEY  
CHIEF BANKRUPTCY JUDGE